E. CONTRIBUTIONS DEDUCTIBILITY AND RELATED MATTERS OF IMPORTANCE FOR EXEMPT ORGANIZATIONS SPECIALISTS

1. Introduction

Contribution deductibility issues are under the general jurisdiction of the Income Tax Division of the Associate Chief Counsel (Technical). However, there are times when Exempt Organizations personnel must have knowledge of the IRC 170 and IRC 162 areas to carry out their functions. The purpose of this article is to acquaint Exempt Organizations specialists with important rules in the deductibility area, especially when they are considering determination and examination cases that deal with organizations engaged in fund raising activities. Two excellent IRS publications are Charitable Contributions, Publication 526, and Determining the Value of Donated Property, Publication 561. Both of these publications are revised yearly.

2. Deductibility of Contributions Under IRC 170(a) and IRC 162

A. General

Charitable contributions to IRC 501(c)(3) organizations, except for testing for public safety organizations, are deductible by donors on their federal income tax returns as provided by IRC 170(a)(1). Deductions for contributions to charitable organizations described in IRC 170(b)(1)(A)(i) through (viii), (public charities and private operating foundations) are allowed to the extent that the aggregate of such contributions does not exceed 50 percent of the taxpayer's contribution base for the taxable year. Contributions to private nonoperating foundations and to certain other organizations performing charitable work are allowed to the extent that the aggregate of such contributions does not exceed the lesser of: (1) 20 percent of the taxpayer's contribution base for the taxable year, or (2) the excess of 50 percent of the taxpayer's contribution base for the taxable year over the amount of charitable contributions allowable to organizations described in IRC 170(b)(1)(A)(i) through (viii), determined without regard to IRC 170(b)(1)(C). The contribution base is the adjusted gross income (computed without regard to any net operating loss carryback to the taxable year under IRC 172). Proposed IRC 170 legislative changes in the Tax Reform Act of 1983 (H.R. 4170), being considered in the fall of 1983, include raising the 20 percent limitation regarding contributions to private nonoperating foundations to 30 percent.

B. Charitable Contribution Defined

A charitable contribution is defined in IRC 170(c)(1) and (2) as a contribution or gift to or for the use of a state, a possession of the United States or the District of Columbia, exclusively for public purposes, or to the charitable organizations described above. For a discussion of foreign charities and contributions made for use in foreign countries, see EO CPE Textbook for 1983, page 228, et seq.

This article is primarily concerned with contributions that may or may not be deductible under IRC 170 to organizations described in IRC 501(c)(3) and contributions to such organizations and other exempt organizations that may or may not be deductible under IRC 162(a). However, some contributions to organizations not described in IRC 501(c)(3) may also be deductible under IRC 170. For example, contributions to an IRC 501(c)(4) organization are deductible under IRC 170 if made to the organization for the use of a state, a possession of the United States, or any political division of the foregoing, the United States, or the District of Columbia, if the contributions are made for exclusively public purposes. Also, certain contributions to organizations of war veterans, domestic fraternal societies, and cemetery companies are deductible. See IRC 170(c)(3), (4), and (5).

Some payments to IRC 501(c)(3) organizations that are not deductible as charitable contributions may be deductible, as are certain payments to other exempt organizations, as trade or business expenses under IRC 162(a). This provision provides for a deduction of all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business. However, IRC 162(b) states that no deduction shall be allowed under IRC 162(a) for any contribution or gift which would be allowable as a deduction under IRC 170 were it not for the percentage limitations, the dollars limitations, or the requirements as to the time of payment as set forth in IRC 170.

To be deductible as a charitable contribution for federal income taxes purposes under IRC 170, a payment to or for the use of a qualified charitable organization must be a gift. To be a gift for such purposes, there must be, among other requirements, a payment of money or transfer of property without adequate consideration. In other words, the transfer must be gratuitous in nature. This is not the case with deductions under IRC 162. A business expense may be deductible even if it is fully quid-pro-quo in nature. Under IRC 170, if the donor receives something of value for a payment, then all or part of the payment will not be a gift and a deduction in whole or in part will not be allowed. Further, if the payment is a

gift, but it is not made for charitable purposes, a deduction for the payment will also be disallowed. For example, contributions earmarked for lobbying are not deductible under IRC 170(c)(2). See Rev. Rul. 80-275, 1980-2 C.B. 69 and discussion later in this topic.

C. Rev. Proc. 82-39 and IRC 7428

Publication No. 78, Cumulative List of Organizations described in Section 170(c) of the Internal Revenue Code of 1954, is a list of organizations to which contributions are deductible. It is published annually by the Internal Revenue Service and updated during the year with three quarterly supplements. Rev. Proc. 82-39, 1982-2 C.B. 759, explains the extent to which contributors may rely on the listing. In order for contributions by donors to be deductible, the organization must qualify at the time of contribution as an organization described in IRC 170(c). When an organization listed in or covered by Publication No. 78 ceases to qualify as an organization, contributions to which are deductible under IRC 170, and the Service subsequently revokes a ruling or determination letter previously issued to it, contributions made to the organization by persons unaware of the change in the status of the organization generally will be considered allowable if made on or before the date of an appropriate public announcement, such as publication in the Internal Revenue Bulletin, stating that contributions are no longer deductible.

However, the Service is not precluded from disallowing a deduction for any contribution made after an organization ceases to qualify under IRC 170, where the contributor: (1) had knowledge of the revocation of the ruling or determination letter; (2) was aware that such revocation was imminent; or (3) was in part responsible for, or was aware of, the activities or deficiencies on the part of the organization that gave rise to the loss of qualification.

Rev. Proc. 82-39 also states that once an organization has received a final ruling or determination letter classifying it as an organization described in IRC 509(a)(1), (2), or (3), the organizations described in IRC 170(b)(1)(A)(i) through (viii) except (vii), the treatment of contributions and grants to such organization under IRC 170, and other Code sections not here relevant, will not be affected by reason of a subsequent revocation by the Service of the organization's classification under IRC 509(a)(1), (2), or (3), until the date on which notice of change of status is made to the public.

Rev. Proc. 82-39 also states that IRC 7428 creates a remedy under declaratory judgment procedures, in part, for cases involving a determination by

the Service with respect to the continuing qualification of an organization as one described in IRC 170(c)(2) or 501(c)(3), or to the continuing classification of an organization under IRC 509(a). The remedy is available in these cases when: (1) the Service determines that revocation of exemption under IRC 501(c)(3), deductibility status under IRC 170(c)(2), or public charity status under IRC 509(a) is appropriate; (2) the organization has exhausted its rights to file a protest and have a conference as set out in Rev. Proc. 80-25, 1980-1 C.B. 667; and (3) the Service has issued a final adverse determination letter to the organization.

IRC 7428(c) of the Code provides for the "validation of certain contributions" made during the pendency of a proceeding for a declaratory judgment involving the revocation of a determination that the organization is described in IRC 170(c)(2). Under this provision, contributions from individuals (up to a maximum of $1,000) and from other charitable organizations described in IRC 170(c)(2) may continue to be deductible. Statutory protection for such contributions, if declaratory judgment is sought on the revocation action, would begin on the date of publication of the revocation and end on the date on which the court first determines that the organization is not described in IRC 170(c)(2). This reliance, however, is not extended to any individual who was responsible, in whole or in part, for the activities (or failure to act) on the part of the organization that were the basis for the revocation.

3. Erroneous Information By Organizations Concerning Deductions

A. Nonexempt Organizations

Erroneous or misleading information is often given by organizations to their contributors under various circumstances. The most blatant situation is where organizations inform their contributors that contributions are deductible as charitable contributions, when the organizations have received rulings or determination letters from the Service holding that they do not qualify for exemption as charitable organizations.

B. Exempt Organizations

False or misleading information by exempt organizations to contributors can be given in various ways: through written or broadcast advertisements of their fund raising events; by word-of-mouth; and by furnishing receipts with erroneous or misleading statements as to deductibility of a "contribution" as discussed below.

(1) Fund Raising

One example of a charitable organization issuing erroneous information is where the organization issues a receipt overstating the amount of a payment that qualifies as a charitable contribution. This situation often arises in connection with fund raising events, where, for example, a person, desiring to financially assist an organization in conducting its charitable activities purchases a ticket to an event sponsored by the organization. The event may be a dinner-dance, a sports event, or the like. Under these circumstances, the purchaser of the ticket receives something of value for the price of the ticket. Generally, the amount paid for the ticket or for some other privilege or benefit is not deductible, in whole or in part, as a charitable contribution, even if the purchaser of the ticket does not attend the event or does not accept the benefit or privilege that the payment bestows. The test of deductibility is not whether the right to admissions or privilege is exercised, but whether the right was accepted or rejected by the donor. Rev. Rul. 67-246, 1967-2 C.B. 104. In some situations none of the payment constitutes a charitable contribution. Rev. Rul. 83-130, 1983-36 I.R.B. 5, states that taxpayers, who purchased raffle tickets on a house from an IRC 501(c)(3) organization received a chance to win a valuable prize, and therefore, received full consideration for the payments. The revenue ruling holds that the purchasers of the raffle tickets may not deduct the cost of the tickets as charitable contributions under IRC 170.

In some cases a portion of the payment made by the donor may qualify as a charitable deduction. As stated in Rev. Rul. 67-246, when something of value has been received by the donor, there is a presumption that there has been no gift and the burden is on the donor to establish that the amount paid is not the purchase price of the ticket or the privilege or benefit received and that part of the payment, in fact, does qualify as a gift. To establish it, an essential element of proof is that the portion of the payment claimed as a gift represents the excess of the total amount paid, over the value of the consideration received. It may be established by evidence that the payment exceeds the fair market value of the privilege or other benefit received by the amount claimed to have been paid as a gift. The 1982 EO CPE Textbook reproduces Rev. Rul. 67-246 at page 158 et seq.

When a fund raising activity is designed to solicit payments, that are intended to be in part a gift, and, in part, the purchase of admission to or other participation in an event of the type in question, the organization conducting the activity should employ procedures that make it clear not only that a gift is being solicited in connection with the sale of an admission or other privilege related to the fund raising event, but also the amount of the gift being solicited. This

procedure requires determining in advance of solicitation the amount properly attributable to the purchase of admissions or other privileges and the amount solicited as a gift. As provided by Rev. Rul. 67-246:

> In making such a determination, the full fair market value of the admission and other benefits or privileges must be taken into account. Where the affair is reasonably comparable to events for which there are established charges for admission, such as theatrical or athletic performances, the established charges should be treated as fixing the fair market value of the admission or privilege. Where the amount paid is the same as the standard admission charge there is, of course, no deductible contribution, regardless of the intention of the parties. Where the event has no such counterpart, only that portion of the payment which exceeds a reasonable estimate of the fair market value of the admission or other privileges may be designated as a charitable contribution.

The respective amounts should be stated at the time of the solicitation and indicated on any ticket, receipt, or other evidence issued in connection with the payment.

It would seem that merely affixing a statement to the solicitation, receipt, etc., to the effect that "contributions are tax deductible to the extent authorized under federal, state, or local law" is not in compliance with the procedure required by Rev. Rul. 67-246.

Application of the principles mentioned above is illustrated by 12 examples in Rev. Rul. 67-246 showing various types of fund raising activities.

In general, here, as in other "contribution" situations discussed in this article, problems may arise during an examination of the returns of the individual or corporation making the donation. Consider, for example, a public television station's fund raising appeal that states: "For your tax deductible contribution of $ 50, we will send you a director's chair premium." If John Q. Public, taxpayer, responds with a non-earmarked check made out to the organization and later claims the full amount of the check as a tax deductible item, notwithstanding contrary instructions attached to the Form 1040, it may not be obvious to a return examiner that there is anything wrong with the deduction. This makes it especially important for Exempt Organizations specialists to advise the offending organization pursuant to the procedure described later in this article at 4.A.(1).

(2) Donations of Articles and Property

Bazaars are used as fund raisers by many charitable organizations and articles offered for sale at the bazaars are often donated by persons interested in supporting the organizations' charitable programs. Some of these articles are relatively inexpensive and some are not. Jewelry, rare artifacts and works of art are often donated to museums and art galleries. Used utilitarian items are often donated to exempt thrift shops.

Reg. 1.170A-1(c) provides that if a charitable contribution is made in property other than money, the amount of the contribution is the fair market value of the property at the time of contribution reduced as provided in IRC 170(e) and paragraph (a) of Reg. 1.170A-4 or IRC 170(e)(3) and paragraph (c) of Reg. 1.170A-4A. The fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts. Rev. Proc. 66-49, 1966-2 C.B. 1257, provides information and guidelines for taxpayers and others with regard to appraisals of contributed property for federal income tax purposes. See also Publication 561.

It should also be noted that if a taxpayer contributes property that would have resulted in gain that would not have been a long-term capital gain if the property had been sold at its fair market value on the date of the contribution, the amount of the contribution must be reduced by the amount of the gain. See IRC 170(e)(1)(A).

(3) Membership Fees

Another example of a donor receiving something of value for a contribution arises in connection with the deductibility of membership dues and fees paid to charitable organizations. Whether the payments are charitable contributions, in whole or in part, is a question of fact and depends on such factors as the nature and extent of the benefits or privileges conferred upon its members. If any reasonably commensurate return privileges or facilities are made available by reason of a membership payment, the payment is not a charitable contribution, except perhaps partly, within the meaning of IRC 170. See Rev. Rul. 68-432, 1968-2 C.B. 104. It is noted, however, that many charities characterize donations as membership dues, when in fact there is little, if any, benefit to contributors. See also Characterization of Contributions discussed at (9) of this part.

(4) Tuition Payments

Tuition payments sometimes give rise to an IRC 170 deduction issue. Tuition payments to IRC 170(c) schools by taxpayers for their children do not constitute charitable contributions because they are personal expenses of the parents. They are not gifts. They are payments to schools for education services rendered to the parents' children. Rev. Rul. 83-104, 1983-30 I.R.B. 5, presents several factual situations that illustrate the distinction between qualified charitable contributions and tuition payments made to an organization that operates an exempt IRC 501(c)(3) private school. Sometimes the distinction is not obvious. For example, situation 3 in the revenue ruling concludes that a payment of $ 400x to a private school is not a charitable contribution where the school admits or readmits a significantly larger percentage of applicants whose parents have made contributions than applicants whose parents have not made contributions. The revenue ruling points out, however, that this conclusion would not result if the preference given to children of contributors is principally due to some other reason. This is a "facts and circumstances" area.

As Rev. Rul. 83-104 explains, usually payments made by a taxpayer on behalf of children attending parochial or other church-sponsored schools are not allowable deductions as charitable contributions either to the school or to the religious organization operating the school if the payments are earmarked for such children. However, the fact that the payments are not earmarked does not necessarily mean that the payments are deductible.

(5) Lobbying

A contribution to an IRC 170(c)(2) organization for lobbying is not deductible. Rev. Rul. 80-275, 1980-2 C.B. 69, holds that a deduction is not allowable under IRC 170 for amounts paid to such an organization that are earmarked for use in, or in connection with, influencing specific legislation. Often a message advertisement that is published for lobbying purposes and calls for "tax deductible contributions to bring the message to others" gives rise to this issue. See examples of lobbying advertisements in the 1978 EO ATRI at page 91, et seq. Issue oriented educational organizations in the military defense, public morality, and environmental areas often publish such advertising. This may also indicate lobbying expenditures subject to IRC 4911 taxation (public charities which have made the IRC 501(h) election) or IRC 4945 taxation (private foundations). This is

a controversial "facts and circumstances" area. This principle is also applicable to gifts "earmarked" for other noncharitable or nonexempt purposes or activities.

(6) "Laundering" - Contributions Paid to a Charitable Organization but Earmarked for Another Organization

If a donor makes a contribution to an IRC 501(c)(3) organization with the understanding that the organization will turn the money over to another organization, as for example an IRC 501(c)(4) organization, to be used by that organization for a non-charitable purpose, such as lobbying, the contribution will not be deductible under IRC 170. Section 3.03 of Rev. Proc. 82-39, supra, provides that the advance assurance of deductibility and public charity status does not apply to contributions or grants made nominally to an organization listed in or covered by Publication No. 78, but with the understanding or on a condition that they be made available to or for the use of an organization not listed in or covered by Publication No. 78.

(7) Contributions to Charitable Organization Deductible under IRC 162

There are situations when a donor who makes a contribution to an IRC 501(c)(3) organization may be entitled to a deduction under IRC 162(a). Rev. Rul. 72-314, 1972-1 C. B. 44, gives an example of such a situation. The payments were made to a charitable organization by a corporation engaged in a stock brokerage business. The purposes of the charitable organization were to reduce neighborhood tensions and combat community deterioration in a neighborhood in which the office of the corporation was located. The amount of the payment equalled six percent of all brokerage commissions received by the corporation. They were made to promote business in the neighborhood and the corporation emphasized in its advertisements to its customers and potential customers that its payments to the charitable organization would enable them to benefit the charitable organization and the community without incurring additional expenses. The revenue ruling holds that the payments were deductible as ordinary and necessary business expenses under IRC 162(a), because they were related to the corporation's business and could reasonably be expected to commensurately further such business financially. This distinction between an IRC 162(a) and an IRC 170(c)(2) deduction is important because under IRC 170(b)(2) a corporation's total charitable deduction for any taxable year may not exceed 10 percent of a corporation's taxable income.

(8) Contributions to Other Exempt Organizations Deductible under IRC 162

Payments to exempt organizations that qualify for IRC 162(e) deductions are usually made to labor organizations under IRC 501(c)(5) and to business leagues under IRC 501(c)(6). These organizations represent labor and businesses and dues and other payments to them by their members further the members' business or professional interests, or their working conditions. These payments may be deductible when used for lobbying purposes, but only if the amounts expended are for direct lobbying on germane matters and for communicating with members on such matters. IRC 162(e)(2) disallows a business expense deduction for amounts expended on political campaign activities or "grassroot" (indirect) lobbying on any matter. See Rev. Ruls. 78-111 through 78-114, 1978-1 C.B. 41 through 44, extracted in the 1981 EO CPE at page 200, et seq. The same rules apply to contributions to IRC 501(c)(4) organizations. See Rev. Rul. 67-163, 1967-1 C.B. 43.

(9) Characterization of Contributions

As noted above, specialists should consider the proper characterization of "contributions", "dues", or "admissions", etc. Often, for example, the so-called "contribution" may be an admission to an event or educational function such as to a museum exhibit. The use of such terminology may indicate that the organization is including such payments as IRC 170(b)(1)(A)(vi) support instead of IRC 509(a)(2) support. IRC 509(a)(2) would be the proper classification. It provides a one-third investment income restriction that is not applicable under IRC 170(b)(1)(A)(vi). In other words, improper characterization of quid-pro-quo income as gratuitous support may be a ploy to avoid private foundation status. Also, "contributions" that are in reality income in exchange for services, goods, raffle or lottery tickets, etc., may indicate an unreported regularly carried on unrelated trade or business subject to IRC 511 tax. See Disabled American Veterans v. U. S. 46 AFTR 2d 80-5438 (Ct. Cl. 1980); U. S. Claims Court, 81-1 USTC 9443, May 20, 1981. See 1982 EO CPE, pages 123, 155.

4. Remedies Available to the Service to Prevent Misleading or Erroneous Information from Being Given to the Public

A. Administrative Remedies

(1) IRM Procedures

The Internal Revenue Manual contains procedures to be taken when an exempt organization gives improper or misleading information regarding the deductibility of contributions to it. IRM 7(10)65.3 (extracted as IRM 7(10)63.6 in the 1982 EO CPE Textbook, page 157), pertains to charitable fund raising affairs where organizations advise the public with erroneous or misleading advertisements that the entire amount paid for tickets or other privileges or benefits is deductible. This IRM provision states that when such advertisements are noted by district offices, sponsors of the event should be promptly contacted by the appropriate key district office and informed of the provisions of Rev. Rul. 67-246. Sponsors should be furnished a formal letter enclosing a copy of the revenue ruling and explaining the substantive rule governing the deductibility of a payment where the donor receives some consideration for it.

When the solicitations in advertisements are a flagrant disregard of the law or regulations, or sponsors of fund raising affairs have refused to cooperate with the Service and persist in misleading the public, an appropriate news release should be issued warning potential patrons that they may not rely on such statements. However, concurrence of the Assistant Commissioner (EP/EO) should be obtained by phone prior to releasing any such notice to the general public.

There may be circumstances when consideration should be given to notifying appropriate state officials, but no action should be taken without clearance through the Disclosure Coordinator. In People of the State of New York v. Life Science Church, 82-1 USTC 9414 (1982), the New York Supreme Court granted the Attorney General of the State of New York a permanent injunction enjoining the respondent Church from illegal and deceptive practices that included misrepresentation of federal tax exempt status.

(2) Examinations of Tax Returns

When, during the course of an examination, an EO specialist finds that an exempt organization is giving false or misleading information to taxpayers about contributions, he or she should inform responsible officials of the organization of the appropriate rules governing the deductibility of contributions and furnish them with a letter similar to the one mentioned in IRM 7(10)65.3. In addition to, or in lieu of Rev. Rul. 67-246, a copy of a more pertinent revenue ruling or a pertinent revenue procedure should be sent as an enclosure to the letter. For example, if members of a charitable organization are receiving some benefit for their dues or fees and they have not been properly informed that all or part of their dues or fees

are not deductible, there should be sent as an enclosure to the letter a copy of Rev. Rul. 68-432 which contains criteria to be applied in determining whether payments in the form of membership dues may be, in whole or in part, deductible as charitable contributions. The organization should be urged to notify its members of the amount of their membership dues or fees that are deductible.

Similar action should be taken in other situations such as when contributions in property are made (furnish a copy of Rev. Proc. 66-49); contributions earmarked for lobbying expenses (furnish a copy of Rev. Rul. 80-275); or where tuition payments are being treated as deductible charitable contributions by the taxpayers (furnish a copy of Rev. Rul. 83-104); raffle ticket situations (furnish a copy of Rev. Rul. 83-130); or in cases involving public interest law firms (furnish a copy of Rev. Proc. 71-39, 1971-2 C.B. 275).

With regard to membership organizations such as IRC 501(c)(5) and 501(c)(6) organizations, IRM 7(10)(11)1, which explains what types of payments by members are lobbying expenditures that are deductible under IRC 162(e)(1), states that if, during the examination of the return of a contributor to an organization located in another district, there are indications that the organization is substantially engaged in the activities specified in Reg. 1.162-20(c)(3), that is, political campaign activities or indirect lobbying activities described in IRC 162(e)(2), the National Office EP/EO Operations Division (OP:E:O:S) should be notified. This notification should describe such activities, the amount of dues or other payments by the contributors, and any other pertinent information available. IRM 7(10)(11)1 contains other detailed instructions regarding examinations of organizations to determine the applicability of Reg. 1.162-20(c)(3) that should be carefully followed.

(3) Caveats in Favorable Rulings and Determination Letters

When a favorable exemption ruling is issued to a fund raising or membership organization and there is an indication that deductibility issues are present an appropriate caveat in the ruling or determination letter should alert the organization to a potential problem that hopefully can be avoided at the outset. See EO CPE 1982 for a discussion of "deductibility and fund raising" on pages 156, 173, and 174, with suggested "pattern paragraphs" for use when appropriate. The "pattern paragraphs" may be tailored to fit particular facts and circumstances. Comparable caveats should also be prepared for IRC 501(c)(5) and (6) organizations when there is evidence of "grassroots" lobbying or political campaign activity.

B. Legal Remedies

(1) Criminal Sanctions

While the Service can take certain administrative actions, as described above, when organizations are misleading their contributors, specific legal action such as revocation of exemption, imposition of penalties, and court action for injunctive relief usually cannot be taken except in very abusive situations. For example, in the case where the Service rules that an organization is not qualified to receive tax deductible contributions and the organization nevertheless informs its contributors that their contributions are tax deductible, IRC 7206(2) appears to be the most likely provision of the Code that would form the basis of legal action against such an organization. That section provides that any person who --

> [w]illfully aids or assists in, or procures, counsels, or advises the preparation or presentation under, or in connection with any matter arising under the internal revenue laws, of a return, affidavit claim, or other document, which is fraudulent or is false as to any material matter, whether or not such falsity or fraud is with the knowledge or consent of the person authorized or required to present such return, affidavit, claim, or document ***

shall be guilty of a felony and, upon conviction thereof, shall be fined not more than $100,000 ($500,000 in the case of a corporation) or imprisoned not more than 3 years, or both, together with the costs of prosecution.

However, inasmuch as this is a criminal provision of the Code, its availability to discourage misstatements by organizations about the deductibility of contributions would appear to present formidable difficulties of proof, etc., in any attempt to use it to prevent the making of such misstatements. The use of such a provision to discourage such misleading statements would be an extreme measure except in the most flagrant case. This is particularly evident when the organization is only lax in indicating to recipients that only a portion of their contributions are deductible.

C. Injunctive Relief

(1) General

A stronger case could perhaps be made for action under IRC 7402 where a representative of an organization informs contributors that their gifts will be tax deductible knowing that the organization is not qualified to receive tax deductible contributions and has reason to believe at the time he or she makes the statement that the contributors will rely on the statement in making their returns. In this type of case, a federal court may have jurisdiction to grant injunctive relief under IRC 7402(a) and 28 U.S.C. 1345.

In an appropriate case it appears that an injunction could be issued. See United States v. Republic Steel Corp., 362 U.S. 482 (1960); In re Debs, 158 U.S. 564 (1895). For the Service to prevail in seeking an injunction, it would have to show injury and an inadequate remedy at law. See Sampson v. Murray, 415 U.S. 61, 88 (1974); Beacon Theaters Inc., v. Westover, 359 U.S. 500, 506-507 (1959). To establish these elements, the government would have to prove that:

1. the organization holds itself out to large numbers of taxpayers as being qualified to receive tax deductible contributions;

2. on the basis of available evidence the organization is not qualified to receive tax deductible contributions; and

3. it is reasonable to conclude that taxpayers will take federal tax deductions based on these misrepresentations.

While various factors have to be considered in seeking injunctive relief, it is apparent that in some cases, especially in flagrant abuse cases, an injunction could be available to the government to prevent misrepresentations in the future. This is a "gray" area without precedent in the exempt organizations area.

(2) Temporary Restraining Order

In some cases where immediate action to stop misrepresentations is desired, a temporary restraining order or preliminary injunction may be sought under Fed. R. Civ. P. 65(b) and (a) respectively, as a prelude to a permanent injunction. To obtain such temporary or preliminary relief, the government must show that: (1) a substantial likelihood exists that the government will ultimately prevail on the merits; (2) the government (or the public) will suffer irreparable injury unless the

injunction issues; (3) the threatened damage to the government (or to the public) outweighs any damage the injunction might cause the opposing party; and (4) the injunction, if issued, would not be adverse to the public interest. State of Texas v. Seatrain International, S.A., 518 F. 2d 175-179 (5th Cir. 1975). This also is a "gray" area.

D. Other Possible Relief

(1) Mail Fraud Issues

Also, prosecution under 18 U.S.C. 1341 (mail fraud) might be appropriate where it can be shown that those making misleading statements through the mails were proceeding willfully and not in good faith. This type of action requires proof of criminal intent, which can be difficult to establish. More likely to be successful are actions under 39 U.S.C. 3005 and 3007. The former section permits the Postal Service to initiate administrative proceedings leading to a "mail stop order" where evidence indicates the existence of a "scheme or device" to obtain money or property by mail by means of a false representation. An attempt to solicit funds by mail which involves false representation of the recipient's tax exempt status would appear to be such a scheme or device. A "mail stop order" prevents the person conducting the challenged solicitation from receiving responsive mail. In appropriate cases, the Postal Service can, under 39 U.S.C. 3007, obtain a district court order allowing them to detain mail addressed to the promoter of a challenged solicitation pending termination of the proceeding under 39 U.S.C. 3005. Should Exempt Organizations specialists have reason to believe that these statutes are being violated, they should bring the matter to the attention of the Chief Postal Inspector, U. S. Postal Service, Washington, DC 20260.

Other areas where there may be evidence of abuse of the nonprofit postal rates, such as exempt organizations using these rates for their taxable unrelated trade or business adjuncts, should, perhaps also be brought to the attention of the U. S. Postal Service.

(2) Cease and Desist Orders - FTC

Also, the Federal Trade Commission may be able to institute administrative proceedings leading to cease and desist orders against a limited class of organizations misrepresenting their status. This action would be based on the Commission's judgment that such misrepresentations constitute an unfair or deceptive practice under the Federal Trade Commission Act. 15 U.S.C. 41, et seq.

The limited availability of this procedure is due to Section 4 and 5 of that Act. 15 U.S.C. 44 and 45. Under these provisions the Commission can proceed against only those corporations, including trusts, organized to carry on business for their own profit or that of their members, or against persons or partnerships.

If consultation with another governmental agency, such as the FTC, the U. S. Postal Service, etc., is being considered, no action should be taken without first clearing the matter through the Disclosure Coordinator.

5. Referral to Examination Division

In cases where an organization is described in IRC 170(c)(2) and contributions to it are deductible, but there is evidence that some payments do not qualify as charitable contributions, in whole or in part, because some consideration was received by the contributors and the organization acts or fails to act in a way that misleads the contributors into understanding that the payments constitute deductible charitable contributions, action to seek injunctive relief generally is not feasible. However, technically speaking, the Service has an adequate remedy at law. It can examine donors' returns and disallow any deduction erroneously claimed.

Recent newspaper reports indicate that some exempt museums may have been providing inflated values to specific donors, for contribution deductibility purposes, of gifts of jewelry, antiques, and fine art. When this sort of practice is discovered during the examination of an exempt organization, the Exempt Organizations specialist should refer the names of the donors to the Examination Division having jurisdiction over the donors, in addition to following the procedures under IRM 7(10)65.3 and discussed above at 4.A.(1).